Brent Christensen 10/04/2007 01:47:17 PM From DB/Inbox: Brent Christensen

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UNCLAS SAN SALVADOR 01964

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UNCLAS SECTION 01 OF 02 SAN SALVADOR 001964

SIPDIS

DEPT FOR WHA/CEN, EEB/TPP/ABT GARY A. CLEMENTS
COMMERCE FOR ITA/OTEXA MARIA D'ANDREA, 4332/ITA/MAC/WH/MSEIGELMAN
STATE PASS TO USTR FOR CAROYL MILLER

E.O. 12958: N/A
TAGS: ECON ETRD KTEX ES
SUBJECT: CAFTA HELPING STABILIZE SALVADORAN MAQUILA SECTOR

REF: A. STATE 114799 B. SAN SALVADOR 001779
¶C. SAN SALVADOR 001423

¶1. SUMMARY: El Salvador's textile and apparel industry is showing signs of greater stability in 2007 after two years of decline following the end of global textile quotas. As reported in reftel B, CAFTA-DR has helped to attract new investment in the maquila sector. The extension of Free Trade Zone benefits (ref C) and U.S. restrictions on Chinese textile imports have also helped Salvadoran maquilas. The textile/apparel industry is adapting to increasing competition by shifting towards full-package production and vertical integration. New investments suggest that CAFTA-DR will help Salvadoran maquilas remain competitive with Asian producers. Nevertheless, many Salvadoran garment producers remain vulnerable to Asian competition, particularly when US restrictions on Chinese textile exports expire in 2008. In response to reftel A, post is providing data for El Salvador in paragraph 2. END SUMMARY.

Textile and Apparel Production and Trade Statistics

¶2. Statistics requested in Ref A are from GOES sources except where indicated:

-- Total industrial production was $3.87 billion for 2006 and $1.03 billion in the first quarter of 2007.

-- Textile and apparel production accounted for $503 million in 2006 and $134 million in the first quarter of 2007 in value-added terms, the only production statistic available. The industry averaged 24.15% value-added in maquila exports from 1996-2006.

-- Textile/apparel imports declined from 20.52% of total imports in 2005 to 15.78% in 2006. Exports of textiles and apparel fell from 53.59% of total exports in 2005 to 45.60% in 2006.

-- Textile and apparel exports to the U.S. were $1,432 million in 2006 and $841.5 million during January-July of 2007 (an 8.3% increase over the same period in 2006) (Source: US Census Bureau)

-- Total manufacturing employment was estimated at 465,760 in 2006; the textile and apparel industry accounted for approximately 81,000 jobs at year-end.

Maquilas Showing Signs of Recovery

¶3. According to GOES statistics, textile exports fell by 1% in the first semester of 2007 from the same period in 2006, following sharper declines of 5.6% in 2005 and 11.7% in 2006. Imports to the textile/apparel sector grew by 5% for the same period suggesting that textile production may rise during the second semester of 2007. Marta Chan, the Acting Executive Director of the Textile and Apparel Industry Association (CAMTEX) questioned the reliability of GOES statistics which are based on customs declarations. CAMTEX instead uses U.S. trade statistics which showed a 10.6% rise in Salvadoran textile/apparel exports to the U.S. during the first semester of 2007 from the same period in 2006.

¶4. The GOES projected in August that textile and apparel exports will grow by 16% in 2007. CAMTEX has set a more modest objective of recovering to pre-CAFTA production levels during 2007. Chan pointed out that 2007 export statistics reflect a recovery from temporary disruption of textile trade in 2006 caused by delayed implementation of CAFTA in some countries that supply thread and cloth to Salvadoran maquilas. (Comment: CAMTEX goals appear more realistic than GOES projections which predict 33% export growth during the second semester of 2007. End comment)

¶4. As reported in ref B, CAFTA has helped draw increasing investment into El Salvador's textile and apparel sector. The National Investment Promotion Agency (PROESA) informed post that new maquila sector investment increased from $35 million in 2006 to at least $325 million in 2007, including two major investments in fabric production: a $200 million investment recently announced by Hanes Brands International (HBI) and a $95 million investment by Pettenati, a Brazilian firm. As new investment has increased, closures of uncompetitive maquilas have declined from 30 in 2005-2006, to six closures in 2007. Most of these closures involved Asian investments in low-cost products.

¶5. During a visit by Econoff to a 3,500-employee thermal underwear factory run by HBI, general manager Edgardo Gonzalez commented that CAFTA "levels the playing field" for Central American producers. Noting that HBI operates in many countries, he suggested that HBI's recent commitment to invest $200 million to acquire and expand a Salvadoran fabric producer, "says a lot about the country and the region". Gonzalez underscored the high productivity of HBI's Salvadoran facilities which have recently outperformed HBI's Honduran facilities in productivity indicators that are prominently posted above the production floor. Gonzalez also praised PROESA for their active efforts to attract investment.

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¶6. El Salvador's garment industry is continuing to adapt to a changing market conditions following the end of the quota regime and implementation of CAFTA. Producers have confirmed that prices and demand have declined since the end of the quota regime, but CAFTA has helped to mitigate this trend. Increased competition has not affected wages since most maquilas combine the legal minimum wage (currently $157.25 per month) with incentive pay. Although Chan said that U.S. restrictions on Chinese textile imports have helped Salvadoran producers, they underscored that Salvadoran maquilas also face stiff competition from south Asian producers. Textile and apparel producers have adapted to increased price competition by expanding full-package services, emphasizing other competitive advantages and pursuing vertical integration.

¶10. COMMENT: New investment highlights continuing promise of

Salvador's textile industry. Although maquila exports may show modest recovery in 2007, smaller firms remain vulnerable to foreign competition. GOES and CAMTEX hope that new investments and a continuing shift toward vertical integration and more competitive maquilas will make up for further closures after U.S. restrictions on Chinese textile imports expire in 2008. END COMMENT

Glazer